



FEDERAL ELECTION COMMISSION  
WASHINGTON, D.C. 20463

August 13, 2008

**MEMORANDUM**

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Chief Compliance Officer

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Assistant Staff Director

**FROM:** Christopher Hughey  
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**SUBJECT:** Interim Audit Report on Tennessee Republican Party (LRA # 745)

**I. INTRODUCTION**

The Office of General Counsel has reviewed the Interim Audit Report ("Proposed Report") on the Tennessee Republican Party ("TRP"). We offer the following comments regarding Finding 3 (Excessive Coordinated Party Expenditures) and Finding 4 (Disclosure of Expenditures for Salary and Wages) in the Proposed Report. The Audit Division raised issues about these two findings in its cover memorandum for the Proposed Report. We commented on these findings informally in meetings and electronic messages, and this memorandum memorializes our comments. We concur with any findings and issues related to the Proposed Report not specifically addressed in this memorandum. If you have any questions, please contact Delanie DeWitt Painter, the attorney assigned to this audit.<sup>1</sup>

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<sup>1</sup> This Office recommends that the Commission consider this document in Executive Session because the Commission may eventually decide to pursue an investigation of matters contained in the Proposed Report. 11 C.F.R. §§ 2.4(a) and (b)(6).

## **II. ADDITIONAL INFORMATION IS NEEDED ABOUT DIRECT MAIL (Finding 3)**

The Proposed Report concludes that TRP exceeded the coordinated party expenditure limits by \$721,093 because it paid for direct mail supporting Bob Corker for Senate which, the auditors contend, meets the content and common vendor conduct standards for coordinated expenditures. *See* 11 C.F.R. §§ 109.37, 109.21. TRP assigned its coordinated party expenditure limitation to the National Republican Senatorial Committee ("NRSC") on September 1, 2006, and the NRSC spent most of the combined limit on media supporting Bob Corker for Senate. TRP incurred \$721,093 in disbursements to a vendor, Creative Direct, LLC, between September and November 2006 for numerous direct mail pieces, which appear to support Bob Corker or to be in opposition to his opponent, Congressman Harold Ford, Jr. Bob Corker's campaign used the same vendor, Creative Direct, for \$680,570 in direct mail between April and September 2006.<sup>2</sup>

To be considered a coordinated expenditure, an expenditure must satisfy both the content and conduct standards. *See* 11 C.F.R. §§ 109.37, 109.21. After reviewing the Proposed Report, we met with the Audit staff and explained that substantial additional information is necessary to support a conclusion that these expenditures meet the "common vendor" conduct standard for coordinated expenditures. *See* 11 C.F.R. §§ 109.37(a)(3), 109.21(d)(4). We suggested that you send letters to TRP and its direct mail vendor, Creative Direct, to clarify whether there was sufficient evidence of coordination to support this finding. We also suggested that you apply the content standard for public communications at section 109.37(a)(2)(iii) to these mailings, if possible, rather than the express advocacy content standard of section 109.37(a)(2)(ii).

The responses from TRP and Creative Direct indicate that they considered the direct mailings to be exempt volunteer activities. TRP states:

We thought these were exempt. We had an official candidate, it was in the General, all processed and stamped in Tennessee, it was non-allocable, paid with Tennessee Victory funds, used volunteers.

Thus, TRP has raised the "volunteer materials" exemption from the definition of contribution and expenditure. *See* 2 U.S.C. § 431(8)(B)(ix) and (9)(B)(viii); 11 C.F.R. §§ 100.87 and 100.147. If the direct mail pieces qualify for the volunteer materials exemption, the possible "common vendor" coordination issue would be immaterial and TRP would not have exceeded the coordinated party expenditure limitations by paying for the direct mail. On the other hand, if they do not qualify for the volunteer materials exemption, the common vendor issue remains live. TRP and Corker used a common vendor; the common vendor developed mailings for both TRP and Corker; and, in response to direct inquiries, neither TRP nor Creative Direct denied the use of information about Corker's plans, projects, activities or needs or claimed the existence of a firewall. Instead, they claimed the activity was exempt, and because exempt activity may be coordinated without limit, a mistaken impression that the activity was exempt may indicate that there was coordination.

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<sup>2</sup> The NRSC also used Creative Direct for a coordinated expenditure in early September 2006.

**A. Recommended Changes to Law and Analysis**

We recommend that you include the following language in the Proposed Report describing the legal requirements for the volunteer materials exemption.

The Act limits the amount that a state party committee may contribute to or spend on behalf of a federal candidate. 2 U.S.C. § 441a(a)(2)(A), 441a(d). The Act, however, also exempts from the definition of "contribution" or "expenditure" campaign materials distributed in connection with volunteer activities when the state party distributes the materials on behalf of a federal candidate of that party. See 2 U.S.C. § 431(8)(B)(ix) and (9)(B)(viii); 11 C.F.R. §§ 100.87 and 100.147. Thus, a state committee may spend an unlimited amount on campaign materials that qualify for the volunteer materials exemption.

To qualify for the volunteer materials exemption, the state party committee's payment for the materials must meet a number of conditions, three of which are particularly important here. First, the committee's payment must not be for the costs of "general public communications or political advertising," which includes "direct mail." 11 C.F.R. §§ 100.87(a) and 100.147(a). "Direct Mail" is defined as any mailing by a commercial vendor or from commercial lists. *Id.* Second, the materials must be "distributed by volunteers and not by commercial or for-profit operations."<sup>3</sup> 11 C.F.R. §§ 100.87(d) and 100.147(d). Third, the exemption does not apply to materials purchased by the national party committee. 11 C.F.R. §§ 100.87(g) and 100.147(g). The remaining conditions are: 1) the portion of the payment allocable to federal candidates must be paid with federal funds; 2) payment must not be from funds designated by the donor for a particular federal candidate; and 3) the payment must be reported as a disbursement. 11 C.F.R. §§ 100.87(b), (c) and (e) and 100.147(b), (c) and (e).

The Commission has interpreted mailings to qualify for the exemption if there was sufficient volunteer involvement even if there was some involvement by a commercial vendor. In past matters, the Commission "emphasized that a 'substantial volunteer involvement' is required [for] the volunteer materials exemption to apply." MUR 5837 (Missouri Democratic State Committee) Statement of Reasons of Commissioners Lenhard, Mason, von Spakovsky and Weintraub, Dec. 20, 2007, at 4. The Commission has considered the "totality of the volunteer involvement in evaluating whether a mailer was 'distributed' by volunteers or was commercial 'direct mail.'" *Id.* at note 3. The question of whether there was substantial volunteer involvement depends on the specific facts and circumstances of the case. The Commission has not absolutely required any specific type of volunteer activity in all cases.

Recently, in MUR 5837, the Commission found that the "amount of volunteer activity involved in bundling, bagging, tagging, and loading the mailers onto a USPS truck constitutes

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<sup>3</sup> Congress intended that the exemption apply only to materials distributed by volunteers because "the purpose of the volunteer materials exemption is to encourage volunteers to work for and with local and State political party organizations;" thus, "[s]ince the purpose is to encourage volunteer participation, distribution by commercial or for-profit operations is not exempted." H.R. Rep. No. 422, 96<sup>th</sup> Cong., 1<sup>st</sup> Sess. 9 (1979).

'substantial volunteer involvement' in the distribution of the mailers and that activity is sufficient to meet the requirements of a volunteer exempt mailing under sections 100.87(d) and 100.147(d)." *Id.* at 4. The Commission noted that even though postage and labels were printed commercially, that did not diminish the volunteer work on the "most important tasks related to 'distribution' – separation and delivery." *Id.* In another recent matter, the Commission noted that while "delivery to the Postal Service by volunteers is a relevant factor . . . it is not dispositive" of whether there was sufficient volunteer activity.<sup>4</sup> MURs 5824 and 5825 (Pennsylvania Democratic State Committee) Statement of Reasons of Commissioners Lenhard, Mason and Weintraub, Jan. 2, 2008 at 6. The Commission concluded that the exemption applied because of "the substantial amount of volunteer involvement in distributing the mailers, including unpacking, bundling, sorting, bagging, tagging, wrapping and loading the mailers" onto trucks hired to transport the mailers to the Postal Service, "as well as presenting them to a Postal Service employee on-site for weighing." *Id.*; *see also* MUR 5841 (Arizona Democratic Party) (Commission found no reason to believe where addresses and postage were commercially printed and volunteers bundled, sorted by zip code, bagged and tagged mailers, but did not transport them to the Post office.)

Conversely, the Commission has concluded in some older matters that the exemption did not apply because volunteers were not sufficiently involved in distributing the mailers. *See, e.g.*, MUR 2559 (Oregon Republican Party) (volunteers stamped nonprofit mail seals, repackaged the brochures and sent them back to the commercial vendor for labeling, sorting by carrier route, tying, sacking, and delivery to the post office); *see also* MUR 2288 (Shimizu for Congress) (volunteers only applied a nonprofit mail seal to the printed material while all other functions were performed afterward by a commercial vendor).

#### **B. Recommended Changes to Recommendation**

We also recommend that the recommendation in Finding 3 be revised to seek additional information from the Committee to demonstrate that the volunteer materials exemption applies to these direct mail pieces. The recommendation should request information about the volunteer activities, and whether any national party funds were used to pay for the mailers. Specifically, the recommendation should request information about whether there was substantial volunteer involvement and whether the volunteers did any of the following separation and distribution activities for the mailers: unpacking, bundling, sorting by zip code or other types of sorting, bagging, tagging, wrapping, loading, weighing, or delivering the mailers to the Post Office.

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<sup>4</sup> In a number of previous enforcement cases, delivery of mailers by volunteers to the post office was a significant factor in determining that the volunteer exemption applied. *See, e.g.*, MUR 4538 (Alabama Republican Party) (volunteers hand stamped the mail indicia and took the mailers to the post office). However, that factor is not dispositive.

### III. APPLICATION OF NEW ALLOCATION RULES FOR STAFF SALARY (Finding 4)

The Audit staff requests our comments on their application of the new and old rules for the payment of staff salary with federal, non-federal or an allocation of federal and non-federal funds depending on the amount of time staff spent on activity related to federal elections. *See* 11 C.F.R §§ 106.7(c)(1), (d)(1) and (2), (e)(2) and 300.33(d); *see also* 11 C.F.R § 100.24(b)(4). This is the first audit to apply the new rules for allocation of salaries, wages and benefits for state party committees, which became effective on January 19, 2006.<sup>5</sup> *See Explanation and Justification, "State, District and Local Party Committee Payment of Certain Salaries and Wages,"* 70 Fed. Reg. 75379 (Dec. 20, 2005). The audit period of January 1, 2005 through December 31, 2006 covers activity both before and after the effective date of the new rule. We generally concur with the application of the old and new rules in the Proposed Report but recommend two changes to this finding. First, the recommendation in this finding should explain that an affidavit would be sufficient to document employee activity only if it describes the particular employee's job duties and activities. Second, the auditors should explain why there was no funding of federal activity by TRP's non-federal accounts.

In general, the Proposed Report correctly applies both the new and old staff salary allocation rules. Under the new rule, state party committees like TRP must pay the salaries, wages and benefits of employees who spend 25% or less of their time in a month on federal election activity or activity in connection with a federal election either entirely with funds from their federal account or allocate the expenses between their federal and non-federal accounts using the allocation method for administrative expenses at section 106.7(d)(2). *See* 11 C.F.R. §§ 106.7(c)(1), (d)(1) and (2), (e)(2) and 300.33(d); 70 Fed. Reg. 75379-82. The new rule also clarifies that state parties must allocate fringe benefits in the same way as salaries and wages.<sup>6</sup> 70 Fed. Reg. 75382. Under the old rule, party committees could use non-federal funds for the salaries, wages and benefits of employees who spent less than 25% of their time on federal activities. Both old and new rules require party committees to keep a monthly log of the time each employee spends in connection with a federal election. The non-federal account may pay the salaries of staff who spent none of their time (0%) on federal election activities. Services provided by state party committee employees who spend 25% or more of their time on activities in connection with a federal election are federal election activity ("FEA") and must be paid with federal funds. 11 C.F.R. §§ 100.24(b)(4), 300.33(d)(2).

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<sup>5</sup> The Commission amended these rules at its discretion following the *Shays* appellate court decision that the Commission had not provided an adequate explanation of its former rules under the Administrative Procedure Act. 70 Fed. Reg. 75379; *see Shays v. FEC*, 414 F.3d 76 (D.C. Cir. 2005). We suggest that you revise the Proposed Report to use this description of the rulemaking rather than stating that the *Shays* court "struck down" the old rule.

<sup>6</sup> The Audit staff explained that the Proposed Report does not address any employee fringe benefits in addition to the salary and payroll tax payments because the auditors did not identify any TRP disbursements for employee fringe benefits.

The Proposed Report correctly applies the new and old rules for employees who spent between 0-25% of their time on federal election activity. To apply the correct rule for employees who spent less than 25% of their time on federal election-related activities, the auditors first considered whether salary and tax payments occurred before the effective date of the new rule (January 19, 2006) and then considered whether there was a monthly log, time sheet or affidavit stating the amount of time spent by the employees on federal activity. We concur that where TRP has not provided sufficient documentation of how employees spent their time, salaries of those employees should be considered non-allocable federal election activity that must be paid with federal funds, like the salaries of employees who spent more than 25% of their time on activities in connection with federal elections. Committees must maintain a monthly log of the percentage of time each employee spends in connection with a federal election. 11 C.F.R. § 106.7(d)(1). Where, as here, a committee fails to do so, and does not provide any other sufficient documentation of how employees spent their time, it is reasonable to treat salaries of those employees as non-allocable federal election activity.

While we agree with this overall approach, we recommend that the Proposed Report be revised to clarify what constitutes sufficient documentation in the absence of a monthly log. TRP will have the opportunity to provide sufficient documentation of employee activity in response to the Interim Audit Report. Although the regulation requires party committees to keep a monthly log, the auditors found that TRP did not maintain monthly logs or time sheets for employees. TRP provided affidavits from four employees, which appear to be signed forms stating that they spent less than or equal to 25% of their time on federal activities. Such affidavits are not sufficient documentation. Form affidavits with only a broad statement that an employee spent less than 25% of time on federal election-related activity are not sufficient evidence because they do not provide information about that employee's actual job duties and activities. We recommend that the salary payments related to these affidavits be treated like other payments that lack sufficient documentation of employee activity.

To be sufficient documentation, an affidavit should describe the individual employee's job duties and activities and explain how the employee allocated their time between federal election activity and other activity. For example, an affidavit would be sufficient if it stated that an employee primarily worked on state legislature campaigns, described the employee's job duties and title and then stated that the employee thus spent less than 25% of her time on activity related to federal elections.

The auditors note that they have not previously required this degree of specificity in such affidavits. Rather, they have allowed form affidavits with general information. We believe, however, that a form affidavit is not sufficient to meet the requirement that a committee must maintain a monthly log of the percentage of time each employee spends in connection with a federal election. 11 C.F.R. § 106.7(d)(1). In order for the Commission to accept an audited committee's affidavit instead of the required monthly log, the affidavit should provide information similar to a monthly log about employee activities. Therefore, we recommend that the recommendation in the Proposed Report be revised to clarify what would constitute a sufficient affidavit.

Memorandum to Joseph F. Stoltz  
Interim Audit Report  
Tennessee Republican Party (LRA 745)  
Page 7 of 7

Finally, the Proposed Report states, "there was no funding of federal activity by the non-federal accounts." The auditors explained to us that there were adequate federal funds to prevent non-federal funding of federal activity. We suggest that the Proposed Report be revised to include a more detailed explanation of why the auditors concluded that no non-federal funds were used for federal activity.